

## **Second Integrated Road Investment Program (i-Road II) - 2018**

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The audit of financial statements of the Second Integrated Road Investment Program- (i-Road II) for the first accounting year ended 31 December 2018 was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Section 4.03 of Article IV of the Loan Agreement No. 3579 SRI and Loan Agreement No. 3580 SRI (COL) dated 22 November 2017 entered into between the Democratic Socialist Republic of Sri Lanka and the Asian Development Bank. My comments and observations which I consider should be report to Parliament appear in this report.

### **1.2 Implementation, Objectives, Funding and Duration of the Project**

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According to the Loan Agreements, then Ministry of Higher Education & Highways, presently the Ministry of Highways & Road Development and Petroleum Resource Development is the Executing Agency and the Road Development Authority is the Implementing Agency of the Program. The objective of the Program is to enhance the road accessibility between rural communities and socio economics centres. The long term impact is to increase transport efficiency of national and provincial roads. The activities of the Project are implemented under 05 components namely civil works, consultancy works, project management unit, utility shifting, taxes, interest and commitment chargers. As per the Loan Agreements, the estimated total cost of the Project amounted to US\$ 1,084.60 million equivalent to Rs. 384,382 million and out of that US\$ 900 million equivalent to Rs. 153,000 million was agreed to be financed by Asian Development Bank. The balance amount of Rs. 31,382 million is expected to be financed by the Government of Sri Lanka. The Project commenced its activities on 20 July 2018 and scheduled to be completed by 19 July 2028.

### **1.3 Qualified Opinion**

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In my opinion, except for the effects of the matters described in the table 2.1 of this report, the accompanying financial statements give a true and fair view of the financial position of the Project as at 31 December 2018, financial performance and its cash flows for the year then ended in accordance with the Sri Lanka Public Sector Accounting Standards.

### **1.4 Basis for Opinion**

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I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

### **1.5 Responsibilities of management and those charged with governance for the Financial Statements**

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Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Public Sector Accounting Standards, and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Program ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Program or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Program's financial reporting process.

The Program is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared by the Program.

## **1.6 Auditor's Responsibilities for the audit of the Financial Statements**

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My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control of the Program.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

I communicate with those charged with governance regarding, among other matters, significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

## 2. Comments on Financial Statements

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### 2.1 Accounting Deficiency

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<b>Accounting Deficiency</b>	<b>Amount Rs. million</b>	<b>Impact</b>	<b>Response of the Management</b>	<b>Auditor's Recommendation</b>
According to the records maintained by the External Resources Department, the disbursement amounting to Rs.2,992.16 million had been made during the year under review. However, the corresponding disbursements amounting to Rs.3,761.08 million had been shown in the financial statements of the Program.	768.92	Un reconciled balances	Not responded	The corresponding figures are needed to be periodically reconciled.

### 3. Physical Performance

#### 3.1 Physical progress of the activities of the Project

Component	Activity	As at 31 December 2018		Audit Issue	Impact	Reason for Delays
		Expected physical performance	Performance Achieved			
Civil Works	(i) Rehabilitation of 400 km of National Roads in the Northern, Eastern, Uva and Western Provinces.			The activity had not been commenced up to 31 December 2018	Possibility to extend the period of the Project and increase of the cost of contract.	Not explained
	(ii) Rehabilitation of 3,750 km of rural Roads in the Northern, Eastern, Uva and Western Provinces	20.7 per cent physical performance from 1,048 km Roads in the Uva Province.	13.8 per cent physical performance from 1,048 km roads in the Uva Province.	The rehabilitation works of the road in other provinces had not been commenced as at 31 December 2018.	Extra Interest and commitment charges may be imposed. Expected outcome of road accessibility to the residents may not be achieved in timely manner.	Financial difficulties faced by the contractors and adverse whether condition.
<b>Response of the Management</b>	Action had been taken to improve the physical progress or otherwise contractual action will be taken.					
<b>Auditor's Recommendations</b>	Activities of the Project are required to be clearly identified through activity plans to achieve the objectives within the targeted period.					

### 3.2 Contract Administration

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The following observations are made.

Audit Issue	Impact	Response of the Management	Auditor's Recommendations
(a) The contractors are allowed to retain the equipment procured to facilitate the staff of the Road Development Authority and the allocation aggregating Rs.87.20 million made to meet the cost thereon as a lump sum basis.	Over estimation of the cost of the contract.	When the ownership of the assets belongs to the contractor at the end of contract period, the contractors bid price consists with reducing the residual values of the particular assets. So there was no adverse impact to the project.	As a general practice, the respective assets are retained by the Employer. Therefore the cost of the contract under this program is required to be reduced, compared with the cost of other contract packages awarded by other Donor Funded Projects.
(b) The bid for the rehabilitation works of the sections of Trincomalee-Batticaloa Road, Allai – Kantalai Road and Coastal Road in the Eastern Province had been called by the Project and evaluation made thereon, without considering the arbitration cases raised by the previous contractor engaged in rehabilitation of the respective sections of the roads under other donor funded project called, Trincomalee Integrated Infrastructure Project. The legal clearance requested from the Attorney General in this regard had not been received even as at 31 December 2018.	Possible dispute on awarding of contracts.	Attorney General Department had given clearance on 15 May 2019 to apply the procurement process.	The Project is required to consider the matter of arbitration cases in order to avoid additional costs.

<p>(c) As per the Sub Clause 4.2 of General Condition of the Contract, the contractors are required to furnish the performance security bonds at their own cost. However, it was observed that the Project had included a separate pay item in the Bill of Quantities to meet cost thereon, contrary to the above mentioned requirement and allowed to contractors to claim the cost incurred on providing of performance security bonds. Accordingly, a sum of Rs.132.80 million had been paid additionally to the contractors engaged in rehabilitation of roads in the Uva Province.</p>	<p>Over estimation of cost of the contractors.</p>	<p>Sub clause 4.2 of General condition of Contract was amended in packages of the Eastern, Northern, Western Provinces accordingly and pay item in the Bill of Quantities was removed.</p>	<p>The review of Bill of Quantities needed to be done by the Procurement Specialist and the Technical Evaluation Committee, before issuing the bidding documents.</p>
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